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Business and Economic Conditions

New York, August, 1957

General Business Conditions

THE month of July has brought no marked change in business activity. As usual, vacation shutdowns have reduced output in some industries, and labor disputes, particularly the long strike in the cement industry, have hampered operations in other areas. In over-all terms, however, the dip seems no more than seasonal. The general trend is still sideways and indecisive, at a high level. Department store sales, seasonally adjusted, appear to have reached a new peak. Steel demand has held up better than expected and automobile production has been greater than last year at this season. On the other hand, demand for nonferrous metals and petroleum products has been sluggish.

Over-all industrial production held on a plateau during the second quarter, with the Federal Reserve Board's index (seasonally adjusted, 1947-49=100) at 143 for April, May and June. This is exactly the figure for August 1956; in the meantime the index marched up to 147 last December, and down again. Any change in July evidently has been small, and this will probably be true for the rest of the summer.

During the spring months trends have varied from one industry to another, but in the aggregate the ups and downs have tended to cancel out in the well recognized process of "rolling readjustment." Recently individual fluctuations have been more moderate than in 1956; last year's precipitous drops in automobiles, home-building, and farm machinery, and sharp rise in producers' goods of all kinds, have had no counterpart in 1957. Rather, activity has leveled out in both firm and soft spots, including such areas of strength as plant and equipment outlays and such areas of weakness as home-building. Similar over-all stability appears in retail sales, which after seasonal adjustment have held within a narrow range of 1 per cent since last November, and in nonagricultural employment (also seasonally adjusted) which has fluctuated less than 1 per cent since the end of the steel strike last August.

The Gain in GNP

On the other hand, the total output of the economy, as measured by the gross national output expressed in dollars, has risen further. According to revised figures published in July, it reached a seasonally adjusted annual rate of $433.5 billion in the second quarter compared with $429.1 billion in the first quarter and $426.0 billion in the fourth quarter of 1956. Price inflation accounted for a major share of the rise, but even so there was a demonstrable increase in over-all activity.

For the divergent trends in the national product, industrial output, and trade, there are several explanations. One is that the service sector of the economy, which is not covered by industrial production and retail sales figures, continuously expands. For example, there were fewer workers

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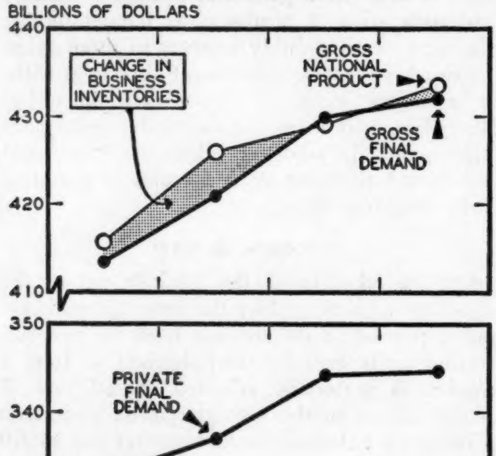
in nonfarm commodity producing industries — manufacturing, mining, and construction in June than a year earlier. But in the broad service industry group — trade, finance, service, and government — employment increased by 600,000 persons during the same period. Growth of services, as well as increased supplies of goods, contribute to a rising standard of living. To that extent the rise in the national product is a gain in real terms.

In other respects, however, the changes in the national product between the first and second quarters of the year are scarcely encouraging. The dollar volume of expenditures for consumer goods (excluding services) and on new construction was unchanged, and expenditures for producers' durable equipment showed a nominal decline, the first since 1954. Adjustments for price increases would reveal moderate real declines in all these categories. The same is true for federal nondefense spending. Thus the $4.4 billion increase in gross national product is accounted for in the main by a revival of inventory accumulation and by continued expansion of government spending on national security and public works. Economic expansion based almost entirely on inventory accumulation and increased government spending is suspect. It is not likely to persist for long nor should it be encouraged to do so.



Gross National Product and Inventory Changes
(Seasonally adjusted annual rate)

Note: Gross national product is the nation's total output of goods and services. Gross final demand equals gross national product minus the change in business inventories. Private final demand equals gross final demand minus government purchases of goods and services.

The slowdown in the private sector of the economy is highlighted in the accompanying chart. For over two years, from the fourth quarter of 1954 to the fourth quarter of 1956, over-all production, as measured by gross national product, consistently exceeded sales to ultimate consumers, as measured by gross final demand. The excess of output over sales went into business inventories, which rose steadily, partly as the natural accompaniment to expanding markets.

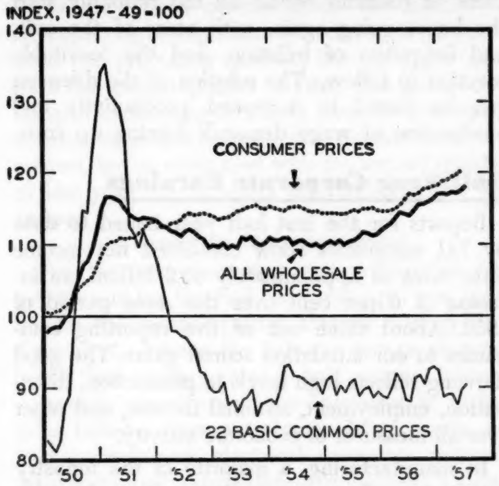
In the first quarter of 1957, gross final demand continued its steady advance, but business men met part of this demand by dipping into stocks while slowing down the rise in output. In the second quarter, however, gross final demand advanced only moderately. With the increase in government spending excluded, private demand was not appreciably greater in the second quarter than in the first. Over-all output continued to rise, with the result that inventories accumulated at the seasonally adjusted rate of $1.5 billion a year. Since farmers' inventories were decreasing at the annual rate of $0.5 billion, nonfarm business stocks increased at a $2.0 billion rate.

The decline in inventories during the first quarter had been regarded by many observers as the beginning of a desirable adjustment. Many had hoped that stocks would be reduced by early fall and that demand for replacement would provide a stimulus in the fourth quarter. Second quarter developments in that respect are disappointing. For some months, purchasing agents have been buying raw materials conservatively, striving to reduce stocks and increase turnover. The resumption of inventory growth under such circumstances indicates that much of the second quarter accumulation may have been involuntary — the backing up of finished goods in the hands of producers. If that is the case, production at some future date will be held back while these stocks are used to fill orders.

Rising Prices and the Consumer

In formulating buying policies, business men seem to have been guided more by the possibility of falling prices, as in most nonferrous metals, than by the prospect of rising prices, as in steel and aluminum. Offsetting movements have kept basic commodity prices fluctuating within a narrow range; the Labor Department's index of 22 basic commodities has shown no consistent trend over the past five years. However, the rise in the general level of prices seems to have accelerated.

Wholesale prices in July showed the sharpest monthly increase since January, rising 0.5 per cent. Most of the price rise occurred in farm products, which reached the highest level since the spring of 1955. The $6 per ton increase in steel prices had only a slight initial impact on over-all industrial prices, but it was sufficient to



Indexes of Consumer, Wholesale, and Basic Commodity Prices (mid-month data)

restore the index to the peak originally reached in February 1957.

The steady advance in consumer prices continued in June and probably into July. The official index (1947-49 = 100) increased 0.5 per cent between May and June, bringing the total rise since March 1956, when the upturn started, to nearly 5 per cent.

Growing public consciousness of price inflation is beginning to cut two ways. Individual purchasing power has lagged, because per capita disposable income has not risen as rapidly as prices during the past year. In addition, the latest study of consumer attitudes by the University of Michigan's Survey Research Center found consumers somewhat less ready to buy than in earlier surveys. They were generally optimistic about their own financial position, and predominantly confident about the general situation, but a somewhat greater percentage than last fall considered prices high and the time less favorable to buy.

Pricing Construction Out of the Market

Outstanding examples of the way in which rising prices have narrowed the market can be found in the construction industry. Selling prices of new homes rose 18 per cent between 1954 and 1956, while members of the National Association of Home Builders report a further rise in 1957 to a median price of $14,800, despite lower profit margins. At this level, a substantial proportion of the nation's families — however much they may want a home of their own — have neither the savings for a downpayment nor sufficient income to meet the costs of home ownership. The situation is most acute in housing, but rising costs have also become important in planning commercial buildings and public works.

There is little doubt about the main cause of higher building costs. Prices of building materials were about the same in June as they were a year ago, while wages in the building trades rose 6 per cent. Moreover, a steady rise in labor costs seems assured for the next few years, since many builders have been obtaining long-term contracts (and perhaps labor peace) at the cost of sizable periodic wage boosts. In New York City, a number of building trades have recently settled for three-year contracts providing for wage increases totaling 65 cents an hour spread at six-month intervals over the life of the contract. There is little likelihood that such large wage increases can be offset by increased productivity. With construction workers in many trades and localities assured of a 10 cent wage boost or better every six months, it is hard to see how the rise in construction costs can be curbed.

So far union negotiators do not appear concerned over the possibility that they may be pricing their members out of the market. However, there are a few straws in the wind. *Engineering News-Record* reports that Dallas plumbers and steamfitters are reducing weekday overtime rates from double time to time and a half in hopes of increasing the number of jobs. But on the whole it is possible that future increases in construction wages will come only at the expense of fewer jobs.

Looking Toward the Fourth Quarter

Expecting no marked change in business before fall, if then, business men are now trying to appraise the outlook for the late months of the year. Latest available figures indicate that, while new orders are in good volume, they are not equal to shipments. Backlogs therefore are declining. This may be only a lull; in any case it is not decisive, for unfilled orders are large even in industries where the trend has been downward for some time. By early fall, however, a pickup will be needed in many lines if output is to be sustained. Meanwhile industrial capacity is increasing. The prospect for more than seasonal improvement in operations is weakened by the change from inventory liquidation to accumulation already noted. If the fall upturn is disappointing, doubts may arise as to the size of plant and equipment expenditures in 1958.

On the other hand, the business changes are moderate, activity in the aggregate holds at or close to record levels, and there is little evidence

of any shift in current thinking sufficient to cause modification of long-range investment programs. The backlog of corporate financing which will come either to the public market or to the banks in the fall is enormous. This persistent demand for business capital, despite higher interest rates, is one of the best indications that plans for expansion and modernization are being carried through. Adding the continuous strength in the service industries and the requirements for highways, schools, and other local government projects, it seems plain that business will have strong support. Moreover, a fourth quarter stimulus from the automobile industry is probable. Competition is acute, new model changes will be substantial and selling efforts vigorous, and more of the people who bought new cars during the 1955 boom should be in the market again.

How these conflicting influences may balance out — in terms of upturn, stability, or downtrend — is not likely to become clear for another couple of months. Another big question is whether rising costs and prices can be passed on, or whether they will limit markets. The anomaly of the present situation is that while there are fewer scarcities of goods and materials and less complete utilization of productive capacity in over-all terms, there is nevertheless steady upward pressure upon costs and prices, and a continuing intense demand for money. The rise in costs and prices has become dangerous both to present economic stability and to future growth. The need of restraint is to be read in the action of the price indexes already cited. If it becomes more difficult to pass on increased costs through higher prices, the result will be fewer jobs. Yet abandonment of restraint would all too probably start the boom going again, with more of the evils and inequities of inflation, and the inevitable reaction to follow. The solution of the dilemma can be found in increased productivity and moderation of wage demands forcing up costs.

Half Year Corporate Earnings

Reports for the first half year issued to date by 741 companies show combined net income after taxes of approximately $6.2 billion, an increase of 6 per cent over the same period of 1956. About three out of five reporting companies in our tabulation scored gains. The good showing reflects high levels in production, distribution, employment, national income, and other over-all measures of economic activity.

In manufacturing, a majority of the industry groups showed increases in both sales and net income. In some lines, however, the rise in operating expenses and taxes absorbed practically all of the increased revenue from sales. A few lines experienced fairly substantial declines in net earnings as a result of the rise in their costs, often combined with a lag in sales.

In fields other than manufacturing, there were half-year increases in net income by the wholesale and retail trade, and the service and amusement industry groups. Continued growth was achieved by the electric, gas, and telephone utilities, but railroads and mining companies showed declines.

The accompanying summary shows by major industry groups the changes for the quarter and half year.

NET INCOME OF LEADING CORPORATIONS FOR THE SECOND QUARTER AND FIRST HALF YEAR

(In Thousands of Dollars)

No. of Cos.	Industrial Groups	Reported Net Income Second Quarter 1956	Reported Net Income Second Quarter 1957	Per Cent Change	Reported Net Income Half Year 1956	Reported Net Income Half Year 1957	Per Cent Change
44	Food products and beverages	$ 82,440	$ 86,186	+ 5	$ 149,784	$ 162,896	+ 9
9	Tobacco products	28,990	33,709	+ 16	53,515	60,039	+ 12
20	Textiles and apparel	11,938	8,639	— 28	29,814	23,300	— 22
28	Paper and allied products	64,787	51,028	— 21	128,194	104,858	— 18
31	Chemical products	186,299	188,392	+ 1	374,656	372,735	— 1
19	Drugs, soap, cosmetics	49,657	53,703	+ 8	102,620	116,291	+ 13
34	Petroleum producing and refining	607,076	714,372	+ 18	1,259,232	1,486,706	+ 18
48	Cement, glass, and stone	107,400	98,788	— 8	193,065	173,515	— 10
35	Iron and steel	300,450	292,551	— 3	581,077	595,025	+ 2
29	Electrical equipment, radio and television	79,699	85,063	+ 7	164,978	179,185	+ 9
49	Machinery	86,598	87,626	+ 1	157,965	170,978	+ 8
93	Other metal products	210,203	172,165	— 18	409,899	341,037	— 17
35	Automobiles and parts	322,767	375,737	+ 16	729,618	826,908	+ 13
28	Other transportation equipment	53,571	58,534	+ 9	99,010	111,416	+ 13
44	Miscellaneous manufacturing	59,852	62,427	+ 4	109,628	115,183	+ 5
546	Total manufacturing	2,251,727	2,368,915	+ 5	4,543,050	4,840,072	+ 7
19	Mining and quarrying	42,764	37,942	— 11	77,939	74,474	— 4
29	Trade (retail and wholesale)	25,309	27,866	+ 10	48,183	55,304	+ 15
21	Service and amusement industries	13,581	15,573	+ 15	26,582	30,245	+ 14
54	Railroads	210,581	154,903	— 26	367,135	319,583	— 13
68	Electric power, gas, etc.	163,583	172,737	+ 6	376,100	395,081	+ 5
4	Telephone and telegraph	195,337	217,560	+ 11	381,467	435,624	+ 14
741	Total	$2,902,932	$2,995,496	+ 3	$5,820,406	$6,150,383	+ 6

For the second quarter alone, net income of all reporting companies was down 5 per cent from the preceding quarter, but up 3 per cent from the second quarter of 1956. The number of companies showing decreases from the preceding quarter exceeded slightly the number with increases, but as compared with the second quarter of last year the increases outnumbered the decreases.

Trends in Manufacturing

For the manufacturing groups together the net income for the half year was up 7 per cent, but for the second quarter alone it was up only 5 per cent. Among the industry groups showing better than average gains in half year net income – usually accompanied by increases in dollar sales billed – were petroleum, drugs, foods, tobacco, machinery, electrical apparatus, automobiles and other transportation equipment. During the second quarter, however, the gains as shown in the table were smaller in most cases.

Rising costs and taxes, often combined with lagging sales, held down the half year gains in several other major lines, while actual declines in half year net income, accompanied in some cases by a falling off in sales billed, were experienced by five groups – textile and apparel, paper, chemicals, cement-glass-stone, and miscellaneous metal products.

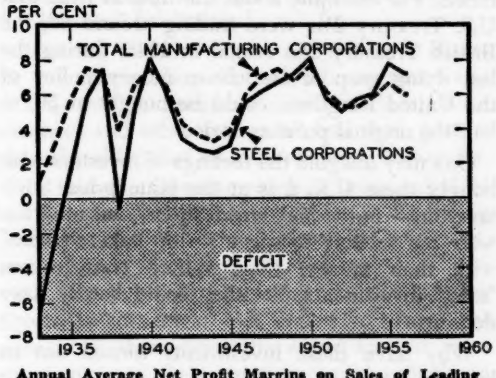
While current reports afford numerous examples of the "profit squeeze" now being commented upon widely, they reveal also that many companies are attaining new high records this year. On the basis of those companies for which comparable sales figures are now available, 8 of the industry groups had narrower margins of net income after taxes to sales, 3 had wider margins, and 4 were practically unchanged. The offsetting effects of combining increases and decreases is to give an over-all average margin that declined slightly from 7.5 to 7.2 cents per sales dollar.

Publicly reported cash dividend payments during the first six months were, according to the U.S. Commerce Department, 4 per cent higher than a year earlier. This against a 16 per cent increase in the first half of '56 over '55.

Profit Margins in Steel

Reports issued to date by 35 iron and steel producers have attracted more than the usual interest because that industry increased wages and prices last month. The number of steel companies having decreases in net income for the half year exceeded slightly the number with increases. Combined net income of the group was up only slightly (2 per cent) despite that industry's peak expenditures of $1.3 billion last year for enlarging plant capacity in order to meet the nation's growing demand for steel products.

Net income of the reporting steel companies in the first half year represented an average margin of 7.9 cents per dollar of sales and other revenues, the same as in the first half of 1956. This compares with 7.2 cents for the full year 1956, pulled down by the steel strike in the third quarter. Such margins are in line with those realized in other periods of active steel production, as may be seen in the accompanying chart based on our annual tabulations of corporate earnings given in the April issues of this Letter.



Annual Average Net Profit Margins on Sales of Leading Companies in the Steel Industry and in the Manufacturing Industries Generally.

The 7.9 cents margin per sales dollar in the first half of this year compares with previous peaks of 7.5 in the full year 1937, 8.1 cents in both 1940 and 1950, and 7.8 cents in 1955.

During the World War II years 1942-45, when steel earnings were held down more than industrial earnings as a whole by rising costs, fixed selling prices, and high taxes, the steel average declined to under 3 cents per sales dollar.

For the entire 24-year period 1933-56 covered by our tabulations, the steel industry margin averaged only 4.5 cents per sales dollar, with three years of net deficit – 1933, 1934, and 1938. In 16 of the 24 years, the steel ratio ran below total manufacturing, averaging over the same period 5.6 cents. Excluding the generally depressed 1930's and taking the 17-year period 1940-56, the average margins for steel was 5.7 cents and for total manufacturing 5.9 cents per sales dollar.

British Treasury 2½s at 50

The decline in Government bond prices in recent months has distressed a number of lawmakers on both sides of Capitol Hill. Senator Albert Gore, of Tennessee, expressed his concern this way on the Senate floor June 19:

> Yesterday 22 issues of bonds of the United States Government deteriorated to new lows. Victory bonds [2½ per cent, sold for 100 in 1945] were bid down to 86.2, almost $14 below par. . . .
>
> Yesterday the holders of United States Government bonds suffered losses in value totaling $113,390,344.
>
> Mr. President, the values of Government bonds are deteriorating daily. How long can this continue without the representatives of the people taking action?

What has happened to U.S. Treasury 2½s — however discouraging to Senator Gore and to the holders of these securities — is mild compared to what has happened to bonds with low interest rates issued years ago by some other governments. For example, about the time in June that U.S. Treasury 2½s were trading around 86, the British Treasury 2½s issued in 1946, during the last dying gasp of the cheap money policy of the United Kingdom, could be bought at 50, or half the original purchase price.

One may imagine the feelings of investors who bought these U.K. 2½s at the issue price. Such investors — individuals, institutions, and others — were not seeking to speculate or "take chances" with their money; they wanted conservative, "safe," investments. Yet they could hardly have done worse.

Why have these investments turned out so badly?

One reason is the natural response of bond prices to rising interest rates. In Britain, as in many other countries including the United States, demands for capital to finance the investment boom have been in excess of savings. As a result, interest rates have gone up, with a depressing effect upon prices of existing bonds carrying lower coupons.

But the world-wide shortage of capital is not the only reason for the poor showing of the bond markets everywhere. It is notable that the stock markets generally have not shared this investor disfavor. While prime bonds go begging at heavy discounts, prices of corporate shares are bid up to levels where, despite all the risks inherent in the equity position, returns to the investor are in many cases substantially lower than those available in the gilt-edge market.

In London, reports *New York Times* correspondent Joseph Frayman in his dispatch of July 7, so pronounced has been the drift of capital from gilt-edge bonds into industrial shares that the differential between the yield on 2½ per cent consols and the 30 high grade industrials in *The Financial Times* index has shrunk to less than 1/3 of 1 per cent. This differential — the smallest in years — is all the more impressive as an index of investor dislike for fixed income securities because the immediate outlook does not promise any noteworthy increase in company profits and dividends.

Taxes and Fear of Inflation

The answer is that people do not want to buy investments that yield them nothing after allowance for taxation and creeping inflation. For example, according to the *New York Times* story:

> The contrast in the behavior of the two groups — between gilt-edge securities bearing assured and fixed rates of interest and industrial shares with flexible dividend distribution and a chance of capital gains and losses — reflected the growing feeling of certainty among investors that the renewed inflation would gather impetus. These doubts extended to the efficacy of the Government's measures to halt the inflationary trend.
>
> As a result, small investors sold government stocks [bonds] heavily and invested the proceeds in the shares of industrial companies in the hope that higher dividends and gains in stock market prices would compensate for the fall in the purchasing value of the pound sterling. Big investors also showed their lack of confidence by abstaining from the gilt-edge market despite the bargain prices to which government stocks had sunk.

The sad state of the government securities market in the U.K. is further explained by a leading London investment house:

> The whole problem is at present clouded by an almost complete sales resistance to government securities, which appear to be at the bottom of most investors' lists of posteriorities. Clearly, the main cause of the trouble lies in the barely checked progress of the creeping inflation, which for all the threat it offers to the economy and the hardships it inflicts on some sections of the community, draws nourishment from conditions of full employment and a welfare state, and appears, on balance, to be regarded by the majority as preferable to its antidote.
>
> The argument is, indeed, put forward that, since the pound has been depreciating in the past decade at an average rate of 4¾ per cent per annum, any investment likely to show a total net return on income and capital accounts over a given period of less than this amount is giving a negative yield and should be discarded.

The Cost-Price Push in Britain

This concern over inflation, manifest in the gilt-edge market, is not a matter of investor psychology alone, but is widely shared by British Government officials, economists, and business men. It coincides with a new series of wage and price increases now threatening to undo the effects of the government credit squeeze and other anti-inflationary devices.

The situation, as described by *Wall Street Journal* correspondent Frank K. Linge, has interest for Americans in view of President Eisenhower's plea for "self restraint" on the part of business and labor, and suggestions in other quarters that business hold the line on prices.

A year ago the British Government asked for, and got, a voluntary but largely effective price

freeze, although labor costs continued to creep upward. Now, reports Mr. Linge, the price freeze is cracking apart – largely under the blows of the Government's own nationalized coal and railroad industries.

The story, as told in the *Journal* of July 10, is instructive in view of the debate over inflation now taking place in this country:

> The British Government has just permitted the State-controlled National Coal Board, which runs the nation's mines, to boost prices at the pit by a tidy 8%. That will add the equivalent of $126 million a year to British industry's production costs as well as increasing household bills for gas and electricity. The nationalized railroads will hike freight charges 10% on August 1, a move figured to raise industry's hauling bill about $42 million a year.
>
> Private industry's reaction was swift – and predictable.
>
> The industry-supported Cement Makers Federation has just boosted prices almost a dollar a ton. "Rising costs, including the higher price of coal, make an increase inevitable," intones J. A. E. Reiss, chairman of the Associated Cement Manufacturers, a private concern that a year ago joined other cement producers in agreeing to peg prices for twelve months.
>
> Imperial Chemical Industries, Britain's largest industrial concern, last July froze prices on a wide range of its products. But in the future, says a company spokesman, "prices will be adjusted up or down as demanded by cost and market conditions."
>
> "The increase in coal prices and the new freight charge hike would seem to mark the end of the price plateau," warns an official of the Association of British Chambers of Commerce. "Taken together these two key costs must result in higher prices for many commodities."

Some other state-run enterprises are going even further. They're so jittery over inflation that they're clamoring to hoist prices in anticipation of rising costs. The state-owned London Transport Board, for instance, is pressing for higher fares on buses, underground trains, and some surface railroads "to budget for a big surplus to act as a cushion against future increases in costs" – a practice for which private industry is often denounced.

Significant also was a statement by a Coal Board official attributing the coal price rise to higher costs, plus a desire to finance capital spending out of profits. (Critics of the recent rise in American steel prices kindly take note.) Here again there is irony in finding socialized industries following practices condemned in other circumstances as examples of "corporate greed."

The Chancellor's Warning

Taking cognizance of the growing uneasiness over the economic situation, the Chancellor of the Exchequer, Peter Thorneycroft, in an address on July 10, warned that the nation "must either squarely face the problem of inflation and accept the policies necessary to check and curtail it, or else it must face a continual decline in the value of its currency."

[Two days later the Government announced an increase in interest rates charged on loans to local authorities and the nationalized industries – a move expected to cut house building programs for which local authorities are responsible, as well as discourage spending by the nationalized industries.]

Mr. Thorneycroft pointed out that if a nation paid itself more for doing no more work, as happened last year, price increases would follow as night followed day. "No economic or governmental magic, no system of controls can stop that process," he declared.

Asserting that the answer did not lie in blaming one another, he said the truth was that wage claims, profits, government expenditure, bank advances and other factors all had their part to play. He added that all solutions were unpopular.

He said the Government was being asked to halt inflation and at the same time it was being pressed to spend more on defense, on education, on roads, and in other fields.

All this has a familiar ring. As the London *Economist* observes, "All countries are in the same boat; throughout the world interest rates are rising, and they are rising most quickly in those countries that have lacked sufficient self-discipline in the past to keep inflation in check."

The U.S. Inflation "Whodunit?"

In this country there has been much talk of something mysterious about the inflation of the past year and a half. The idea that there have been "new forces" at work has been broached in three separate Congressional hearings – the Senate Finance Committee investigation of the "financial condition" of the country, the Senate Antitrust subcommittee inquiry into so-called administered prices, and the Joint Economic subcommittee study of tax policies.

Questions have been asked why prices have continued to rise in the face of government budgetary surpluses, tight money, and plentiful supplies of goods. There have been persistent suggestions that "administered prices" are the villain.

Actually, there is no great mystery in why prices have gone up. George M. Humphrey, former Treasury Secretary, in his statement before the Senate Finance Committee on June 18 challenged the theory that big government spending in itself is not inflationary, and that the inflationary pressure comes not from spending but from budgetary deficits. Asserting that

"government expenditures are inflationary, particularly when the economy is at a high level of output and employment," the Secretary explained:

> Taxes divert to government spending some funds which, in the hands of the taxpayer, would have gone into savings. Furthermore, some government expenditures go into payments to produce goods and services (especially military equipment and services) which neither contribute to the nation's capital account nor become available for private consumption. Yet this additional purchasing power competes for the existing supply of goods and services.

Neither is it mysterious that prices have continued to rise in the face of a restrictive monetary policy and a growing plenitude of goods. There is no timetable on the effects of tight money; they operate gradually, and influence some economic sectors more quickly than others. A good deal depends upon public psychology and the extent to which the business and speculative community takes the bit in its teeth. It may be recalled that it required Federal Reserve discount rates as high as 7 per cent in 1920 and 6 per cent in 1929, with open market rates ranging much higher, to check the booms of those years.

Similarly, in prices, response to changing credit conditions and demand-supply relationships is not always immediate, many commodities continuing to rise while others level off or even decline. All this is normal, reflecting the fact that some commodities remain in short supply longer than others, and the known tendency of prices of commodities in relatively advanced stages of fabrication to be "stickier" than others.

"Administered Prices" vs. "Administered Wages"

This brings up the question of "administered prices" that is worrying Senator Estes Kefauver of Tennessee and a good many others. It is an old bogey, conjured up to scare people twenty years ago at the time the TNEC (Temporary National Economic Committee), a Congressional-Administration investigating body, conducted its "monopoly inquiry."

Senator Kefauver, Chairman of the Senate Antitrust subcommittee, makes much of the fact that within a broad area of the economy prices are set, "not automatically by the unseen hand of competition, as are the prices of wheat and hogs, but by the conscious and deliberate action of corporation managers who have the power to set prices at alternative levels."

The question is, how else should these prices be set — by having people haggle over each item as they do in the oriental bazaars?

Neither can corporation managers arbitrarily "set" prices where they want them regardless of market conditions. While, admittedly, there are varying degrees of "stickiness," experienced business men realize full well that prices must in the end conform to what buyers can and will pay regardless of whether sellers like it or not. Witness, for example, the recent action of non-ferrous metals prices which, under the influence of mounting stocks, have fallen well below levels satisfactory to producers; likewise the failure last month, for similar reasons, of fuel oil prices to hold advances posted by the oil companies in hopes of recouping increased wage costs.

Contesting charges by Senator Gore and Professor John K. Galbraith of Harvard, in the Senate Finance Committee hearings, that administered pricing is now the pattern for much of U.S. industry, Secretary Humphrey strongly stated that competitive pricing still exists.

He cited the steel industry as an example. In times like the present, he said, when there is a good supply, the low pricing company sets the prices which all the rest must follow. He noted that several steel executives have complained bitterly that U.S. Steel raised its price by only $6 a ton in June, and have expressed the view that the increase should have been much greater.

The fact is that, when it comes to identifying "new forces" promoting inflationary pressures, there is more to be said for singling out "administered wages." With the labor unions today numbering over 17 million members, as against 3 million a generation ago, holding hundreds of millions of dollars in their treasuries, and exercising under aggressive leadership concentrated power far beyond anything enjoyed by the largest corporations, here indeed is an element of great importance present in larger measure than ever before.

Coupled with the philosophy of full employment under which governments are mandated to maintain conditions maximizing labor's bargaining power, that element is chiefly responsible for the fear of creeping inflation that to an increasing extent is influencing business and investment decisions.

Getting Out on a Limb?

This growing acceptance of the idea of inflation as the new way of life is manifest in the action of the security markets described earlier. More and more, investors tend to disregard tested yardsticks of prudent investment in the effort to hedge against an expected declining value of money. Similarly, many business concerns find in rising construction and equipment costs an in-

ducement for speeding up programs of expansion and other capital improvements that otherwise might be put off to a later date.

This preoccupation with beating inflation is not a wholesome development. The longer it goes on, the greater the danger that a good many people and concerns may find themselves out on a limb should things not pan out as expected. Even though those who predict creeping inflation should prove to be right in the long run, the movement they envisage is hardly likely to proceed without interruptions, which could be painful. With the expansion of industrial capacity that has taken place in many lines, there is some question as to how much further wage and price increases can go without encountering consumer resistance and over-supply, with deflationary results.

Will there be a business reaction in the next year or two? Is the boom running out of steam? As J. Douglas Gibson, Assistant General Manager of the Bank of Nova Scotia and past president of the Canadian Political Science Association, pointed out in an address before the Canadian Gas Association last month, "There are no sure answers to these questions, but they are questions we should not cease to ask." His comments on the need for an attitude of "healthy skepticism" regarding projections of prosperity and creeping inflation were much to the point:

> Up until a year or so ago, businessmen were asking themselves a good many questions about the outlook and this attitude of healthy skepticism did much to prevent excesses which might have got us into trouble. I don't think there is enough questioning going on today. There is too much uncritical acceptance of the indefinite continuance of prosperity; there is too much acceptance of the idea that we are in an era of creeping inflation.

Wanted: $17,000,000,000

The unremitting need in this country for new capital to finance business growth and expansion is illustrated repeatedly in the annual reports for 1956 or fiscal years ended in early '57, now available from practically all of the larger corporations. For the 100 largest industrial companies alone, the indicated outlays of capital last year for new and improved plant and equipment to help meet the country's ever-growing demand for goods amounted to $10.6 billion. In addition there was absorbed in larger inventories, receivables, investments, and other assets (exclusive of cash and government securities) a total of $6.7 billion. Thus to finance these expenditures the companies had to obtain funds – over and above those needed to cover current operating costs for materials, labor, other expenses, and taxes – aggregating $17.3 billion.

Raising sums of such magnitude, even by such a prosperous group of industrial "giants," called for the limitation of corporate dividends to a little over half of the net income last year and the retention of the balance for reinvestment. It caused heavy drains upon corporate holdings of cash and government securities, with a consequent decrease in liquidity. In addition, it involved some increase in outstanding debt and sale of additional equity stock.

The 100 Largest Manufacturers

An accompanying list of the 100 manufacturing corporations reporting the largest total assets as carried on the books at the end of 1956 shows 22 companies now over the $1 billion mark. An additional 40 are over $500 million, with the smallest in the group at $293 million.

Total Assets, 100 Largest Manufacturing Corporations, As Reported at End of 1956 (In Millions)

Allied Chem. & Dye Cp.	$742	Liggett & Myers Tob. Co.	$482
Allis-Chalmers Mfg. Co.	514	Lockheed Aircraft Corp.	385
Aluminum Co. of Amer.	1,158	Monsanto Chemical Co.	598
American Can Co.	500	Natl. Dairy Prod. Corp.	512
American Cyanamid Co.	560	Natl. Distil. & Chem. Cp.	428
Amer. Smelt. & Ref. Co.	435	Natl. Lead Co.	353
American Tobacco Co.	790	Natl. Steel Corp.	675
Anaconda Co.	976	North Amer. Aviation	391
Armco Steel Corp.	613	Ohio Oil Co.	366
Armour & Co.	468	Olin Mathieson Chem. Cp.	654
Atlantic Refining Co.	700	Owens-Illinois Glass Co.	403
Bendix Aviation Corp.	322	Phelps Dodge Corp.	458
Bethlehem Steel Corp.	2,090	Phillips Petroleum Co.	1,373
Boeing Airplane Co.	332	Pitts. Plate Glass Co.	555
Borden Co.	326	Procter & Gamble Co.	554
Borg-Warner Corp.	404	Pure Oil Co.	488
Burlington Industries	488	Radio Corp. of Amer.	691
Caterpillar Tractor Co.	400	Republic Steel Corp.	857
Celanese Corp. of Amer.	335	Reynolds Metals Co.	613
Chrysler Corp.	1,295	R. J. Reynolds Tob. Co.	659
Cities Service Co.	1,198	Richfield Oil Corp.	317
Continental Can Co.	634	St. Regis Paper Co.	299
Continental Oil Co.	549	Schenley Industries	397
Crown Zellerbach Corp.	520	Scott Paper Co.	298
Deere & Co.	446	Shell Oil Co.	1,315
Distillers Cp. - Seagrams	482	Sinclair Oil Corp.	1,473
Douglas Aircraft Co.	357	Singer Mfg. Co.	445
Dow Chemical Co.	646	Skelly Oil Co.	389
E.I. du Pont de N. & Co.	2,364	Socony Mobil Oil Co.	2,820
Eastman Kodak Co.	656	Sperry Rand Corp.	709
Firestone Tire & Rub. Co.	705	Stand. Oil Co. of Calif.	2,041
Ford Motor Co.	2,793	Stand. Oil Co. (Ind.)	2,425
General Amer. Tr. Cp.	333	Stand. Oil Co. (N. J.)	7,902
General Dynamics Corp.	435	Stand. Oil Co. (Ohio)	333
General Electric Co.	2,221	J. P. Stevens & Co.	318
General Foods Corp.	404	Sun Oil Co.	578
General Motors Corp.	6,569	Sunray Mid-Con. Oil Co.	504
B. F. Goodrich Co.	519	Swift & Co.	562
Goodyear Tire & Rub. Co.	852	Texas Company	2,504
W. R. Grace & Co.	433	Tidewater Oil Co.	680
Gulf Oil Corp.	2,872	Union Carbide Corp.	1,460
Inland Steel Co.	572	Union Oil Co. of Calif.	651
Inter. Bus. Mach. Cp.	769	United Aircraft Corp.	376
Inter. Harvester Co.	1,009	United Fruit Co.	401
Inter. Paper Co.	765	U.S. Rubber Co.	609
Inter. Tel. & Tel. Corp.	761	U.S. Steel Corp.	3,836
Jones & Laughlin Stl. Cp.	732	Western Electric Co.	1,224
Kaiser Alum. & Chem. Cp.	519	Westinghouse Elec. Cp.	1,264
Kaiser Steel Corp.	293	Weyerhaeuser Timber Co.	404
Kennecott Copper Corp.	834	Youngstown Sh. & Tube Co.	621

The continued growth of large companies and of industry in general reflects the great postwar program, now in its twelfth year, of capital investment for enlarging the capacity and improving the efficiency of productive facilities. Inflation of prices and wages also has swelled the dollar totals.

Among the major industry groups represented the largest by far is petroleum producing and refining with 21 companies, most of which operate nationally or internationally and whose assets comprise 33 per cent of the combined total. Other leading industry groups in the list are 9 companies in steel, 8 nonferrous metals, 7 chemicals, 8 machinery and equipment, 7 aircraft, 6 food, 5 electrical equipment, 4 tires, and 4 paper. A number of other mass production industries making consumer goods or capital goods are represented by 3 companies or less.

Changes Over the Years

The changing character of American industry is seen from a comparison of this list of leaders today with that of a generation ago – a reminder that a company's membership in the "100 largest" group carries no assurance of permanent status. Going back thirty years to 1926, for example, 41 companies have since disappeared from the list – exclusive of several now operating under changed corporate titles. On the earlier list were but two manufacturers with assets over $1 billion, against 22 today. This wholesale shifting of industrial leaders gives a graphic picture of national growth, corporate enterprise, competition, and changing habits in public demand.

Most of the companies that dropped out of the 1926 list were engaged in older industries where rates of growth have slowed down. They include 2 baking, 4 sugar, 5 other foods, 2 leather and shoes, and 5 railway equipment. Automobile producers in the list declined from 7 to 3.

Of the 41 companies displacing them, most are in the newer and faster-growing industries. There were added 7 aircraft, 6 electrical and other equipment, 5 petroleum, 4 chemical products, and 3 distilling – a "new" industry following prohibition repeal in 1933. In textiles, a leader in woolen goods dropped out but there were 3 newcomers – manufacturers of synthetic yarns or integrated mills using all the major fibres.

Investment $17,000 per Job

To carry on their far-flung operations, the 100 largest manufacturing corporations employed last year a total of 5,638,000 men and women. Thirty-eight of them each employ more than 50,000 people. The combined book assets of the companies, aggregating $94.3 billion at the year end, represent an average of about $17,000 per employe, although the figure varies widely among different industries and among leading producers. This reflects differences both in the degree of mechanization and in accounting methods of valuation.

The book assets average generally in the $5-10,000 range for builders of tires, aircraft, and electrical apparatus, where a relatively high degree of hand labor is necessary in spite of heavy capital outlays on plant and equipment. An investment of $10-15,000 is required by the big food processors, and by automobile and machinery builders, while $15-20,000 is used in textiles, paper, and steel. The still greater capital needed for extensive equipment and mechanization runs $20-30,000 per worker in chemicals and nonferrous metals, and $40-60,000 in petroleum and (including working capital to carry warehouse inventories) in distilling and tobacco products.

This substantial cost for "tools" and the incessant need for their replacement, modernization, and expansion explain the constant demand of business for new capital. Such funds may be obtained from a company's own operations, from its shareholders including its own employes, and from outside banking and investment sources.

Ownership of the equity capital of the 100 largest companies is widely distributed among 7,278,000 registered shareholders. Their equity had a balance sheet value at the year end totaling $61.7 billion, or about two thirds of total assets, while the number of common shares outstanding amounted to 1,874,000,000. Forty-two of the companies each have more than 50,000 shareholders. Sixty-five each have more shareholders than employes.

The combined total of shareholders, of course, contains considerable duplication, because the same investors own stock in more than one company in the group. Some registered shareholders, however, are nominees or trustees acting for large numbers of individual owners as well as for banks, brokers, insurance companies, investment trusts, colleges, churches, foundations, and other institutions. Many of the companies' employes are also shareholders, in addition to which in numerous cases large blocks of stock are held in trust for employes' profit-sharing, pensions, and other purposes. One of the world's largest oil companies in its 1956 report notes that its largest shareholder is the trustee under its employe savings plan holding about 2 per cent of the outstanding shares.

Disposition of Receipts

Last year the 100 largest manufacturing organizations had total receipts aggregating $115.5 billion from sales, other operations, and investments. Thirty-three companies each had receipts exceeding $1 billion, whereas the 1926 list contained only a single company above such level

— attained that year for the first time. Following is a summary, partly estimated, of the disposition of last year's receipts:

Disposition of Receipts by the 100 Largest U.S. Manufacturing Companies in the Year 1956

	Total (Millions)	% of Receipts
Total receipts from sales, revenues, etc.	$115,472	100.0
Costs:		
Costs of goods and services purchased from others, etc.	59,865	51.8
Wages, salaries, and labor benefits*	30,767	26.7
Provision for depreciation and depletion	5,028	4.4
Interest paid	474	.4
Income taxes	6,298	5.5
Other federal, state, local & foreign taxes†	4,670	4.0
Total costs of operations	107,102	92.8
Net income	8,370	7.2
Preferred and common dividends paid	4,374	3.8
Retained in the business	$3,996	3.4

*Partly estimated, on basis of payrolls reported by companies representing 86 per cent of the total employment of the group.

†Tax figures charged as costs are exclusive of various sales and excise taxes collected from customers. Such taxes on gasoline and oil collected by the 21 petroleum companies amounted to $3,588 million, while those collected by the 3 automobile companies came to $1,883 million.

Wages, salaries, and labor benefits (pensions, insurance, hospitalization, paid vacations, etc.) amounted to approximately $30.8 billion or 26.7 cents per sales dollar. Such employment costs represented an average of $5,500 per employe.

Income taxes came to $6.3 billion, while other federal, state, local, and foreign taxes were $4.7 billion. The total direct taxes of $11.0 billion represented an average of 9.5 cents for every dollar of sales, and were over one third as large as payrolls. In addition to such taxes charged as costs, there were sales and excise taxes of $3.5 billion on gasoline and oil collected from customers by the 21 petroleum companies, plus other excises collected by the automobile and other companies.

After deducting all other operating expenses for costs of goods and services purchased from others (a major part of which also went to labor indirectly), for depreciation and depletion of physical properties, and for interest paid on borrowed money, the net income amounted to $8.4 billion or 7.2 cents per sales dollar.

Cash dividends paid to shareholders totaled $4.4 billion or 3.8 cents per sales dollar, while the balance of $4.0 billion or 3.4 cents per sales dollar was retained to finance business growth.

Decline in Liquidity

As already noted, expenditures by these companies last year for plant and equipment, plus funds absorbed by the increase in other assets, totaled $17.3 billion. Although over half of such capital was provided by retained earnings, plus depreciation and depletion allowances, there still remained a wide gap to be financed from other sources. These were mainly cash and marketable securities, increase of debt, and sale of additional capital stock.

As shown in the summary below, these companies' combined holdings of cash and marketable securities (reported mostly as U.S. Governments, but including also some local and foreign governments and other marketables) totaled approximately $13.1 billion at the year end and were down $3.7 billion or 22 per cent.

Cash alone was down only 3 per cent, but marketable securities were down 32 per cent.

(In Millions of Dollars)

	End of Year 1955	1956	Change	% Change
Cash	$ 5,645	$ 5,471	— 174	— 3
Governments, etc.	11,228	7,650	—3,578	—32
Total	$16,873	$13,121	—3,752	—22
Current liabilities	18,903	18,895	— 8	—
Percent	89%	69%		

Meanwhile, total current liabilities standing at $18.9 billion were practically unchanged. The ratio of cash and marketable securities to total current liabilities declined from 89 to 69 per cent.

Rising costs in recent years have increased the capital requirements of all businesses, from the largest down to the smallest. A recent study by Dun & Bradstreet shows that the cost of establishing a new retail business in this country has climbed from an average in 1945-47 of $9,500 to a May 1957 figure of $14,700 — a rise of 55 per cent. To start a wholesale business in the mid-1940's required $22,000, but now takes $31,700 — 44 per cent more.

Future Growth

The tremendous growth of the country's large corporations in the past gives an indication of the further opportunities that may be looked for in the future. But such growth will require more and more people, research, and investment. To meet the demand for petroleum products alone it was estimated recently by an industry spokesman that the new capital needed over the next five years will amount to $60 billion.

There will continue, of course, to be shifts in the position of the business leaders, who are under constant pressure from their competition and whose bigness alone is no guarantee of lasting success. Big business as well as small business must always keep alert to serve the public which, in the last analysis, determines the size which any organization may attain. It is interesting to speculate on the composition of the "100 largest" list, and the magnitude of the figures it will present, when another thirty years will have rolled by.

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